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Department of the Treasury
Internal Revenue Service

Instructions for Form 1120L

U.S. Life Insurance Company Income Tax Return

(Section references are to the Internal Revenue Code, unless otherwise noted.)

Paperwork Reduction Act Notice.—We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that taxpayers are complying with these laws, and to allow us to figure and collect the right amount of tax. You are required to give us this information.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is:

Recordkeeping	69 hrs., 50 min.
Learning about the law or the form	29 hrs., 6 min.
Preparing the form	53 hrs., 51 min.
Copying, assembling, and sending the form to IRS	6 hrs., 26 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form more simple, we would be happy to hear from you. You can write to the **Internal Revenue Service**, Washington, DC 20224, Attention: IRS Reports Clearance Officer, TR:FP; or the **Office of Management and Budget**, Paperwork Reduction Project, Washington, DC 20503.

General Instructions

Purpose of Form.— Form 1120L, U.S. Life Insurance Company Income Tax Return, is used to report income, gains, losses, deductions, and credits of life insurance companies.

Filing Form 1120L

Who Must File.—Every domestic life insurance company and every foreign corporation carrying on an insurance business within the U.S. that would qualify as a life insurance company if it were a U.S. corporation must file a return on Form 1120L. This includes organizations described in section 501(m)(1) that provide commercial-type life insurance.

To qualify as a life insurance company, a company must meet the statutory requirements specified in section 816. The company must be an insurance company engaged in the business of issuing life insurance and annuity contracts and must meet the reserves test specified in section 816(a).

The term "insurance company" means any company more than half of the business of which during the taxable year is the issuing of insurance or annuity contracts or the reinsuring of risks underwritten by insurance companies.

The life insurance business of a company includes the issuance of life insurance and annuity contracts either separately or combined with health and accident insurance, or noncancelable contracts of health and accident insurance. Guaranteed renewable life, health, and accident insurance that the company cannot cancel but under which the company reserves the right to adjust premium rates by classes, according to experience under the kind of policy involved, are treated as noncancelable.

The reserves test requires that the company's life insurance reserves, as defined in section 816(b), plus its unearned premiums and unpaid losses (whether or not ascertained) on noncancelable life, health, or accident policies not included in life insurance reserves, must make up more than 50% of its total reserves as defined in section 816(c). In determining whether a company meets the reserves test, the following modifications must be made: (1) life insurance reserves and total reserves must each be reduced by an amount equal to the mean of the aggregates, at the beginning and end of the taxable year, of the policy loans outstanding with respect to contracts for which life insurance reserves are maintained; (2) amounts set aside and held at interest to satisfy obligations under contracts which do not contain permanent guarantees with respect to life, accident, or health contingencies shall not be included in either life insurance reserves (section 816(c)(1)) or other reserves required by law (section 816(c)(3)); and (3) deficiency reserves shall not be included in either life insurance reserves or total reserves.

Mutual savings bank conducting life insurance business.—Mutual savings banks conducting life insurance business and meeting the requirements of section 594 are subject to an alternative tax consisting of the sum of: (1) a partial tax computed on **Form 1120,** U.S. Corporation Income Tax Return, on the taxable income of the bank determined without regard to income or deductions allocable to the life insurance department, and (2) a partial tax on the taxable income computed on Form 1120L of the life insurance department. Enter the combined tax on line 3 of Schedule J, Form 1120. Attach Form 1120L as a schedule and identify it as such.

Insurance companies other than life insurance companies.—Insurance companies that do not qualify as life insurance companies should file **Form 1120-PC,** U.S. Property and Casualty Insurance Company Income Tax Return. A burial or funeral benefit insurance company that directly manufactures funeral supplies or performs funeral services is taxable under section 831 and should file Form 1120-PC.

When To File

In general, a corporation must file its income tax return by the 15th day of the 3rd month after its tax year ends. A new corporation filing a short period return must generally file by the 15th day of the 3rd month after the short period ends. A corporation that has dissolved must generally file by the 15th day of the 3rd month after the date it dissolved.

A foreign corporation that does not maintain an office or place of business in the U.S. has until the 15th day of the 6th month after the end of its tax year to file.

Extension.—File **Form 7004,** Application for Automatic Extension of Time To File Corporation Income Tax Return, to request an automatic 6-month extension of time to file.

Period Covered.—File the 1988 return for calendar year 1988. Section 843 requires all insurance companies to file on a calendar year basis, unless they join in the filing of a consolidated return. If a consolidated return is filed, the parent return would indicate the period covered.

Final Return, Change of Address, Amended Return.—If this is a final return, or the corporation's address has changed since the previous return was filed, or you are filing an amended return, check the appropriate box.

Where To File.—

If the corporation's principal business, office, or agency is located in ▼	Use the following Internal Revenue Service Center address ▼
New Jersey, New York (New York City and counties of Nassau, Rockland, Suffolk, and Westchester)	Holtsville, NY 00501
New York (all other counties), Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont	Andover, MA 05501
Florida, Georgia, South Carolina	Atlanta, GA 39901
Indiana, Kentucky, Michigan, Ohio, West Virginia	Cincinnati, OH 45999
Kansas, New Mexico, Oklahoma, Texas	Austin, TX 73301
Alaska, Arizona, California (counties of Alpine, Amador, Butte, Calaveras, Colusa, Contra Costa, Del Norte, El Dorado, Glenn, Humboldt, Lake, Lassen, Marin, Mendocino, Modoc, Napa, Nevada, Placer, Plumas, Sacramento, San Joaquin, Shasta, Sierra, Siskiyou, Solano, Sonoma, Sutter, Tehama, Trinity, Yolo, and Yuba), Colorado, Idaho, Montana, Nebraska, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, Wyoming	Ogden, UT 84201
California (all other counties), Hawaii	Fresno, CA 93888
Illinois, Iowa, Minnesota, Missouri, Wisconsin	Kansas City, MO 64999
Alabama, Arkansas, Louisiana, Mississippi, North Carolina, Tennessee	Memphis, TN 37501
Delaware, District of Columbia, Maryland, Pennsylvania, Virginia	Philadelphia, PA 19255

T22.51:

Corporations having their principal place of business outside the United States or claiming a possessions tax credit (section 936) must file with the Internal Revenue Service Center, Philadelphia, PA 19255.

The separate income tax returns of a group of corporations located in several service center regions may be filed with the service center for the area in which the principal office of the managing corporation that keeps all the books and records is located.

Signature.—The return must be signed and dated by the president, vice-president, treasurer, assistant treasurer, chief accounting officer, or any other corporate officer (such as tax officer) authorized to sign. A receiver, trustee, or assignee must sign and date any return required to be filed on behalf of a corporation.

If a corporate officer filled in Form 1120L, the Paid Preparer's space under "Signature of officer" should remain blank. If someone prepares Form 1120L and does not charge the corporation, that person should not sign the return. Certain others who prepare Form 1120L should not sign. For example, a regular, full-time employee of the corporation, such as a clerk, secretary, etc., does not have to sign.

Generally, anyone who is paid to prepare Form 1120L must sign the return and fill in the other blanks in the Paid Preparer's Use Only area of the return.

The preparer required to sign the return MUST complete the required preparer information and:

- Sign it by hand in the space provided for the preparer's signature. (Signature stamps or labels are not acceptable.)
- Give a copy of Form 1120L to the taxpayer in addition to the copy filed with IRS.

Tax return preparers should be familiar with their responsibilities. See **Pub. 1045,** Information for Tax Practitioners, for more details.

Figuring and Paying the Tax

1. Accounting Methods.—You must file the return using the accrual method of accounting or, to the extent permitted under regulations, a combination of the accrual method with any other method, except the cash receipts and disbursements method.

Unless the law specifically permits, you cannot change the method of accounting used to report income in earlier years (for income as a whole or for any material item) unless you first get IRS consent on **Form 3115,** Application for Change in Accounting Method.

2. Rounding Off to Whole-Dollar Amounts.—You may show money items on the return and accompanying schedules as whole-dollar amounts. To do so, drop any amount less than 50 cents and increase any amount from 50 cents through 99 cents to the next higher dollar.

3. Depositary Method of Tax Payment.—The corporation must pay the tax due in full when the return is filed but no later than 2½ months after the end of the tax year.

Deposit corporation income tax payments (and estimated tax payments) with a Federal Tax Deposit Coupon (Form 8109). Be sure to darken the "1120" box on the coupon. Make these tax deposits with either a financial institution qualified as a depositary for Federal taxes or the Federal Reserve bank or branch servicing the geographic area where the corporation is located. Do not submit deposits directly to an IRS office; otherwise, the corporation may be subject to a failure to deposit penalty. Records of deposits will be sent to IRS for crediting to the corporation's account. See the instructions contained in the coupon book (Form 8109) for more information.

To help ensure proper crediting to your account, please write your employer identification number, the type of tax paid, and the tax period to which the deposit applies on your check.

To get more deposit coupons, use the reorder form (Form 8109A) provided in the coupon book.

For more information concerning deposits, see **Pub. 583,** Information for Business Taxpayers.

4. Estimated Tax.—Generally, a corporation must make estimated tax payments if it can expect its estimated tax (income tax minus credits) to be $500 or more. Use **Form 1120-W,** Corporation Estimated Tax, as a worksheet to compute estimated tax. Use the payment coupons (Form 8109) in making deposits of estimated tax.

If the corporation overpaid estimated tax, it may be able to get a "quick refund" by filing **Form 4466,** Corporation Application for Quick Refund of Overpayment of Estimated Tax. The overpayment must be both: (1) at least 10% of expected income tax liability, and (2) at least $500. To apply, file Form 4466 within 2½ months after the end of the tax year and before the corporation files its tax return.

5. Timing Change in Deducting Accrued Expenses.—Generally, an accrual basis taxpayer can deduct accrued expenses in the tax year that all events have occurred that determine the liability, and the amount of the liability can be determined with reasonable accuracy.

Generally, however, all the events that establish liability for the amount are treated as occurring only when economic performance takes place. There are exceptions to this general rule. See section 461(h).

Interest and Penalties

Interest and penalty charges are described below. If a corporation files late or fails to pay the tax when due, it will be liable for penalties unless it can show that failure to file or pay was due to reasonable cause and not willful neglect.

Interest.—Interest is charged on taxes not paid by the due date, even if an extension of time to file is granted. Interest is also charged on penalties imposed for failure to file, negligence, fraud, gross valuation overstatements, and substantial understatements of tax, from the due date (including extensions) to the date of payment. The interest charge is figured at a rate determined under section 6621.

Late Filing of Return.—A corporation that fails to file its return when due (including extensions) may be subject to a penalty of 5% a month or fraction of a month, up to a maximum of 25%, for each month the return is not filed. The penalty is imposed on the net amount due. The minimum penalty for failure to file a tax return within 60 days of the due date for filing (including extensions) is the lesser of the underpayment of tax or $100.

Since Regulations section 1.6012-2(c) requires that the annual statement approved by the National Association of Insurance Commissioners (NAIC) be filed as part of the return, a late filing penalty may be imposed for not including the annual statement when the return is filed.

Late Payment of Tax.—Generally, the penalty for not paying tax when due is ½ of 1% of the unpaid amount, up to a maximum of 25%, for each month or fraction of a month the tax remains unpaid. The penalty is imposed on the net amount due.

Underpayment of Estimated Tax.—A corporation that fails to make estimated tax payments when due may be subject to an underpayment penalty for the period of underpayment. To avoid the estimated tax penalty, the corporation must make estimated tax payments of at least 90% of the tax shown on the return or 100% of its prior year's tax. See section 6655.

Form 2220, Underpayment of Estimated Tax by Corporations, is used to see if the corporation owes a penalty. Generally, the corporation does not have to file this form because IRS can figure the amount of any penalty and bill the corporation for it. However, you must complete and attach Form 2220 even if the corporation does not owe the penalty if: **(a)** the annualized income or adjusted seasonal installment method is used, or **(b)** the corporation is a "large corporation" computing its first required installment based on the prior year's tax. If you attach Form 2220, be sure to check the box on line 16, and enter the amount of any penalty on that line.

Overstated Tax Deposits.—If deposits are overstated, the corporation may be subject to a penalty of 25% of the overstated deposit claim. See section 6656(b).

Other Penalties.—There are also penalties that can be imposed for negligence, substantial understatement of tax, and fraud. See sections 6653 and 6661.

Other Forms, Returns, Schedules, and Statements That May Be Required

1. Forms.—The corporation may have to file any of the following:

Forms W-2 and W-3. Wage and Tax Statement; and Transmittal of Income and Tax Statements.

Form W-2P. Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments.

Form 1096. Annual Summary and Transmittal of U.S. Information Returns.

Form 1098. Mortgage Interest Statement. This form is used to report the receipt from any individual of $600 or more of mortgage interest in the course of the corporation's trade or business for any calendar year.

Forms 1099-A, B, DIV, INT, MISC, OID, PATR, R, and S. Information returns for reporting abandonments, acquisitions through foreclosure, proceeds from brokers and barter exchange transactions, real estate transactions, certain dividends and distributions, interest payments, payments

for certain fishing boat crew members, medical and dental health care payments, direct sales of consumer goods for resale, miscellaneous income payments, nonemployee compensation, original issue discount, patronage dividends, and total distributions from profit-sharing plans, retirement plans, and individual retirement arrangements. Also use these returns to report amounts that were received as a nominee on behalf of another person.

For more information, see **Pub. 916,** Information Returns.

Note: *Every corporation must file information returns if, in the course of its trade or business, it makes payments of rents, commissions, or other fixed or determinable income (see section 6041) totaling $600 or more to any one person during the calendar year.*

Form 5452. Corporate Report of Nontaxable Dividends.

Form 5498. Individual Retirement Arrangement Information. Use this form to report contributions (including rollover contributions) to an individual retirement arrangement (IRA) and the value of an IRA or simplified employee pension account.

Form 5713. International Boycott Report, for persons having operations in or related to "boycotting" countries. In addition, persons who participate in or cooperate with an international boycott may have to complete Schedule A or Schedule B and Schedule C of Form 5713 to compute their loss of the following items: the foreign tax credit, the deferral of earnings of a controlled foreign corporation, IC-DISC benefits, and FSC benefits.

Form 8264. Application for Registration of a Tax Shelter. This form is used by tax shelter organizers to register tax shelters with the IRS for the purpose of receiving a tax shelter registration number.

Form 8271. Investor Reporting of Tax Shelter Registration Number. This form is used by taxpayers who have acquired an interest in a tax shelter, which is required to be registered, to report the tax shelter's registration number.

Form 8271 must be attached to any tax return (including an application for tentative refund (Form 1139) or an amended return) on which a deduction, credit, loss, or other tax benefit attributable to a tax shelter is taken, or any income attributable to a tax shelter is reported.

Form 8281. Information Return for Publicly Offered Original Issue Discount Instruments. This form is generally required to be filed by issuers of public offerings of debt instruments within 30 days of the issuance of the debt instrument.

Form 8300. Report of Cash Payments Over $10,000 Received in a Trade or Business. Generally, this form is used to report the receipt of more than $10,000 in cash or foreign currency in one transaction (or a series of related transactions).

Form 8390. Information Return for Determination of Life Insurance Company Earnings Rate Under Section 809. This form is filed by all mutual life insurance companies and the 50 largest stock life insurance companies, as determined by the Secretary of the Treasury, to gather information to compute the "differential earnings rate."

2. Returns.

Consolidated Returns.—If an affiliated group of corporations includes one or more domestic life insurance companies taxed under section 801, the common parent may elect to treat those companies as includible corporations. The life insurance companies must have been members of the group for the 5 tax years immediately preceding the tax year for which the election is made. See section 1504(c)(2) and Regulations section 1.1502-47(d)(12).

Note: *If an election under section 1504(c)(2) is in effect for an affiliated group for the tax year, all items of members of the group that are not life insurance companies are not to be taken into account in figuring the tentative life insurance company taxable income of members that are life insurance companies.*

The parent corporation of an affiliated group of corporations must attach **Form 851,** Affiliations Schedule, to the consolidated return. For the first year a consolidated return is filed, each subsidiary must attach **Form 1122,** Authorization and Consent of Subsidiary Corporation to be Included in a Consolidated Income Tax Return.

File supporting statements for each corporation included in the consolidated return. Use columns to show the following, both before and after adjustments:

- Items of gross income and deductions.
- A computation of taxable income.
- Balance sheets as of the beginning and end of the tax year.
- A reconciliation of retained earnings.
- A reconciliation of income per books with income per return.

Attach consolidated balance sheets and a reconciliation of consolidated retained earnings.

3. Pension, Profit-Sharing, Etc. Plans.—Employers who maintain a pension, profit-sharing, or other funded deferred compensation plan, whether or not qualified under the Internal Revenue Code and whether or not a deduction is claimed for the current tax year, generally are required to file one of the forms described below. There are penalties for failure to file these forms on time.

In addition there is a penalty for overstating the pension plan deduction. See section 6659A.

Form 5500.—Complete this form for each plan with 100 or more participants.

Form 5500-C or 5500-R.—Complete the applicable form for each plan with fewer than 100 participants.

Form 5500EZ.—Complete this form for a one participant plan.

Note: *Contributions to a pension or annuity plan representing past service costs are now subject to the uniform capitalization rules of section 263A or the long-term contract rules of section 460. Thus, an allocable share of all otherwise allowable pension costs, whether they relate to current or past services, must be included in the basis of property produced or held for resale, including property the taxpayer produces under a long-term contract. This change in the law is effective for costs incurred after 1987 for property (other than inventory) produced by the taxpayer, including costs allocable to long-term contracts under section 460. For inventory costs the change is effective for tax years beginning after 1987, and is treated as a change in accounting method initiated by the taxpayer and made with IRS consent. Any adjustment required under section 481(a) must be included in income over a period not to exceed 4 years.*

4. Statements.

NAIC Annual Statement.—Regulations section 1.6012-2(c) requires that the NAIC Annual Statement be filed with Form 1120L.

Stock ownership in foreign corporations.—Attach the required statement to Form 1120L if the corporation owned 5% or more in value of the outstanding stock of a foreign personal holding company and the corporation was required to include in its gross income any undistributed foreign personal holding company income. See section 551(c).

A corporation that controls a foreign corporation, or that is a 10%-or-more shareholder of a controlled foreign corporation, or acquires, disposes of, or owns 5% or more ownership in the outstanding stock of a foreign corporation may have to file **Form 5471,** Information Return with Respect to a Foreign Corporation.

A domestic corporation or a foreign corporation that is engaged in a trade or business in the United States and is controlled by a foreign person may have to file **Form 5472,** Information Return of a Foreign Owned Corporation.

Transfers to a corporation controlled by the transferor.—If a person receives stock or securities of a corporation in exchange for property, and no gain or loss is recognized under section 351, the person (transferor) and the transferee must attach to Form 1120L the information required by Regulations section 1.351-3.

Attachments.—In order to process the return we ask that you complete every applicable entry space on Form 1120L. Please do not attach statements and write "See attached" in lieu of completing the entry spaces on Form 1120L.

If more space is needed on the forms or schedules, attach separate sheets indicating at the top of each attachment the form number or schedule letter of the form or schedule being continued. Show the same information called for on the form in the same order as on the printed forms. Be sure to show totals on the printed forms. Please use sheets that are the same size as the forms and schedules. Attach these separate sheets after all the schedules and forms. Also, put the corporation's name and employer identification number (EIN) on each sheet.

Sales and Exchanges of Life Insurance Company Property

Capital Assets Defined.—Except for those assets specifically excluded by section 1221, each asset held by a corporation (whether or not the asset is connected with its business) is a capital asset. Section 1221 provides that the term "capital asset" does not include: (1) inventory or property held by the taxpayer primarily for sale to

customers in the ordinary course of the taxpayer's trade or business; (2) depreciable or real property used in the taxpayer's trade or business; (3) certain copyrights, literary, musical or artistic compositions; (4) accounts or notes receivable acquired in the ordinary course of a trade or business for services rendered or from the sale of property described in (1) above; and (5) certain publications of the U.S. Government.

For life insurance companies, section 818(b) modifies the above definition so that only property used in carrying on an insurance business will be considered as "depreciable or real property used in the taxpayer's trade or business." Thus, for life insurance companies, gains or losses from the sale or exchange of depreciable assets of any business other than an insurance business will be treated as gains or losses from the sale or exchange of capital assets.

Capital Gains and Losses.—Report capital gains and losses on **Schedule D (Form 1120)**, Capital Gains and Losses, according to the instructions for that form. Enter on line 6, Schedule C (Form 1120L), the excess of net short-term capital gain over the net long-term capital loss as shown on line 9, Schedule D (Form 1120). Enter on line 5, Schedule A (Form 1120L), the net capital gain shown on line 10, Schedule D (Form 1120). Attach Schedule D (Form 1120) to Form 1120L.

Sales of assets used in a trade or business and involuntary conversions.—Use **Form 4797,** Sales of Business Property, to report gains and losses from sales or exchanges of assets used in a trade or business and from involuntary conversions.

With regard to life insurance companies, section 818(b)(1) provides that, for purposes of section 1231(a), the term "property used in a trade or business" includes only:

1(a). For property acquired before 6/23/84 or after 12/31/87, property used in carrying on an insurance business that is either real property held for more than 1 year or depreciable property held for more than 6 months;

(b). For property acquired after 6/22/84 and before 1/1/88, property used in carrying on an insurance business that is either real property held for more than 6 months or depreciable property held for more than 6 months; and

2. Timber, coal, and domestic iron ore to which section 631 applies.

For purposes of paragraph 1 above, the term "property used in a trade or business" does not include property includible in inventory, property held primarily for sale to customers, or certain copyrights, literary, musical or artistic compositions, letters, memoranda and similar property.

Report ordinary gains and losses from Form 4797 on line 6, Schedule A (Form 1120L).

Note: *New rules apply to installment sales for nondealers of property that is used in a taxpayer's trade or business or held for the production of rental income if the sales price is greater than $150,000. An interest charge is imposed on the tax that is deferred under the installment method to the extent the outstanding face amount of installment obligations arising from all dispositions of such property occurring during any year exceeds $5 million. See section 453A for more information.*

Special rules for section 818(c) property.—See section 818(c) (relating to property held on December 31, 1958, and certain substituted property acquired after December 31, 1958) and the related regulations for how to limit the gain from the sale or exchange of any section 818(c) property.

Foreign life insurance companies.—A foreign life insurance company that sells a U.S. real property interest must file Form 1120L and Schedule D (Form 1120) to report the sale. Gain or loss from the sale of a U.S. real property interest is considered effectively connected with the conduct of a U.S. business, even though the foreign life insurance company does not carry on any insurance business in the U.S. and is not otherwise required to file a U.S. income tax return.

Specific Instructions

Line A

Employer identification number.—Enter the corporation's employer identification number (EIN). A corporation that does not have an EIN should apply for one on **Form SS-4,** Application for Employer Identification Number. This form may be obtained from most IRS and Social Security Administration offices. Send Form SS-4 to the same Internal Revenue Service Center to which Form 1120L is mailed. If the EIN has not been received by the filing time for the corporation, write "Applied for" in the space provided for the EIN.

Line F

Check the box provided if the corporation is a foreign corporation and has made the election under section 953(c)(3)(C) to treat its related person insurance income as effectively connected with the conduct of a trade or business in the United States. A foreign corporation making this election should file its return with the Internal Revenue Service Center, Philadelphia, PA 19255.

Note: *Once made, this election shall apply to the taxable year for which made and to all subsequent taxable years unless revoked with the consent of the Secretary of the Treasury.*

Schedule A — Life Insurance Company Taxable Income (LICTI) (Section 801(b))

Income, Lines 1 through 7

Line 1.—Enter gross premiums and other consideration received on insurance and annuity contracts less return premiums and premiums and other consideration paid for indemnity reinsurance.

Gross premiums and other consideration includes advance premiums, deposits, fees, assessments, consideration received for assuming liabilities under contracts not issued by the company, and any amount treated as premiums received under section 808(e) (see Schedule E instructions below).

Return premiums include amounts rebated or refunded due to policy cancellations or due to incorrectly computed premiums, but do not include amounts returned to policyholders when such amounts are not fixed in the contract but instead depend on the company's experience or the management's discretion.

Line 2. Decrease in reserves.—If there is a decrease in reserves, you cannot complete line 2 until you do the following: (1) pencil in the amount from line 8, Schedule B, on line 2, Schedule A, to tentatively compute life insurance company gross income; (2) use this tentative life insurance company gross income figure to complete Schedule K, Company/Policyholder Share Percentage; and (3) complete Schedule B. After completing steps 1 through 3, above, erase the numbers penciled in for step 1 and then enter on line 2, Schedule A, the net decrease in reserves shown on line 12, Schedule B.

Line 3. 10% of certain decreases in reserves.—Section 807(f)(1) provides that if the amount of any item referred to in section 807(c) decreases as a result of a change in the basis used to determine such item, 10% of the decrease shall be included in life insurance company gross income for each of the 10 succeeding taxable years.

Note: *If a company ceases to qualify as a life insurance company, section 807(f)(2) provides that the balance of any adjustments under section 807(f) shall be taken into account in the last tax year the company is qualified to file Form 1120L.*

Line 6. Other amounts.—Enter the total of all other income not included on lines 1 through 5, if such items are includible in life insurance company gross income. Also include all gains reported on Form 4797.

For mutual life companies, if the recomputed differential earnings amount (determined under section 809(f)(3)) for the preceding taxable year exceeds the differential earnings amount (determined under section 809(a)(3)) for such tax year, the excess should be included on line 6 as other income for the current taxable year.

Attach an itemized schedule of all items included in the entry on line 6.

Deductions, Lines 8 through 14

Line 8. Death benefits, etc.—Enter all claims and benefits accrued and losses incurred (whether or not ascertained) during the year on insurance and annuity contracts. The term "losses incurred (whether or not ascertained)" means a reasonable estimate both of losses incurred but not reported and of losses that have been reported, where the amount of the losses cannot be determined by the end of the taxable year. Losses incurred must be adjusted to take into account any salvage and reinsurance recoveries attributable to those losses together with estimates of salvage and reinsurance that may be recovered on such losses in future years. This estimate includes the estimated value of unaccrued subrogation claims contested by third parties.

Note: *Section 807(c) provides that the amount of the unpaid losses (other than losses on life insurance contracts) shall be the amount of the discounted unpaid losses as defined in section 846. See the instructions on page 6 regarding the discounting provisions.*

Line 10. 10% of certain increases in reserves.—Section 807(f)(1) provides that if the amount of any item referred to in section 807(c) increases as a result of a change in the basis used to determine such

item, then 10% of the increase shall be allowed as a deduction in computing life insurance company taxable income for each of the 10 succeeding taxable years.

Note: *If a company ceases to qualify as a life insurance company, section 807(f)(2) provides that the balance of any adjustments under section 807(f) shall be taken into account in the last year that the company is qualified to file Form 1120L.*

Line 12. Consideration paid for assumption by another person of liabilities under insurance, etc., contracts.—Enter the total consideration paid by the company to another person (other than consideration paid for indemnity reinsurance) for the assumption by such person of liabilities under insurance and annuity contracts (including supplementary contracts).

Line 13. Dividends reimbursable by taxpayer.—Enter the amount of policyholder dividends paid or accrued by another insurance company for policies the taxpayer has reinsured and that are reimbursable by the taxpayer under the terms of the reinsurance contract.

Line 14. Other deductions.—Enter the total of all other deductions (including the amortization of premiums under section 811(b)) not included on lines 8 through 13, to the extent that such items are deductible in computing life insurance company taxable income. Include the total amount of deductions for a noninsurance business (defined in section 806(b)(3)).

Note: *Effective for tax years beginning after December 31, 1987, a deduction for additions to a reserve account for vacation pay is limited to the vacation pay that is paid during the current taxable year or within 2½ months after the close of the taxable year of the employer with respect to which the vacation pay was earned by the employees.*

The change from the reserve method is treated as a change in method of accounting initiated by the taxpayer and made with IRS consent. The net amount of the adjustment required by the change in accounting method equals the excess of the amount in the reserve at the end of the year preceding the year of the change over the amount accrued at the end of the year preceding the year of change and paid within 2½ months after the close of that year. The net amount of the adjustment reduced by the balance in the suspense account under section 463(c) must be included in income as follows: 25% for the year of change, 5% in the first year after the year of change, 35% for the 2nd year after the year of change, and 35% in the 3rd year after the year of change. However, if Rev. Proc. 84-74 1984-2C.B. 736 requires the adjustment to be taken into account over a period of less than 4 years, the adjustment is to be included in income ratably over the shorter period. See section 10201 of the Revenue Act of 1987 ("Act of 1987") for more information.

For mutual life companies, if the differential earnings amount (determined under section 809(a)(3)) for the preceding taxable year exceeds the recomputed differential earnings amount (determined under section 809(f)(3)) for such taxable year, the excess should be included on line 14 as a deduction in computing life insurance company taxable income for the current taxable year.

Attach an itemized schedule of all items included in the entry on line 14. On the attached schedule, deductions attributable to a noninsurance business should be segregated from all other deductions.

If the corporation claims a deduction for depreciation or amortization, attach **Form 4562,** Depreciation and Amortization.

If the corporation claims a deduction for timber depletion, attach **Form T (Timber),** Forest Industries Schedules.

Limitations on Deductions

Charitable contributions.—A deduction is allowed for charitable contributions or gifts actually paid within the tax year to or for the use of charitable and governmental organizations described in section 170(c), and for any unused contributions carried over from prior years.

Corporations on the accrual basis may elect to deduct contributions paid by the 15th day of the 3rd month after the end of the tax year if the contributions are authorized by the board of directors during the tax year. Attach to the return a declaration, signed by an officer, stating that the resolution authorizing the contributions was adopted by the board of directors during the tax year. Also attach a copy of the resolution.

The total deduction allowable in any year may not exceed 10% of life insurance company taxable income computed without regard to:

- the deduction for charitable contributions;
- the deduction for policyholder dividends;
- the deduction for dividends received;
- the small life insurance company deduction;
- any operations loss carryback to the taxable year under section 810; and
- any capital loss carryback to the taxable year under section 1212(a)(1).

Charitable contributions in excess of the 10% limitation may not be deducted in the current taxable year but may be carried over to the next 5 taxable years. A contribution carryover is not allowed, however, to the extent that it increases an operations loss deduction.

Special rule for contributions of certain property.—For a charitable contribution of property, you must reduce the contribution by the sum of:

1. The ordinary income or short-term capital gain that would have resulted if the property had been sold at its fair market value, and
2. All of the long-term capital gain that would have resulted if the property had been sold at its fair market value.

The reduction for long-term capital gain applies to:

1. Contributions of tangible personal property for use by an exempt organization for a purpose or function unrelated to the basis for its exemption; and
2. Contributions of any property (except stock for which market quotations are readily available — see section 170(e)(5)) to or for the use of certain private foundations. (See section 170(e) and Regulations section 1.170A-4.)

For special rules for contributions of inventory and other property to certain organizations, see section 170(e)(3) and Regulations section 1.170A-4A.

Charitable contributions of scientific property used for research.—A corporation (other than a personal holding company or a service organization) can receive a larger deduction for contributing scientific property used for research to an institution of higher education. For further information, see section 170(e).

Documentation required for certain contributions.—For contributions made in property other than money, attach a schedule showing the name of each organization to which such a contribution was made and the amount of the contribution. Describe the kind of property contributed and the method used in determining its fair market value. If you include a contribution carryover, show the amount and how it was determined.

If you made a qualified conservation contribution under section 170(h), include the fair market value of the underlying property before and after the donation. Describe the conservation purpose furthered by your donation and the type of legal interest contributed.

Section 263A uniform capitalization rules.—Many items that were deductible under prior law must now be capitalized or included in inventory under the uniform capitalization rules of section 263A. The rules require corporations to capitalize or include in inventory certain costs incurred in connection with the production of real and personal tangible property held in inventory or held for sale in the ordinary course of business. Tangible personal property produced by a taxpayer includes a film, sound recording, videotape, book, or similar property. The rules also apply to personal property (tangible and intangible) acquired for resale. Taxpayers subject to the rules are required to capitalize not only direct costs but also an allocable portion of most indirect costs (including taxes) that benefit the assets produced or acquired for resale. Interest expense paid or incurred in the course of production must be capitalized and is governed by special rules. The uniform capitalization rules also apply to the production of property constructed by a taxpayer for use in its trade or business or in an activity engaged in for profit.

Section 263A does not apply to personal property acquired for resale if the taxpayer's annual average gross receipts are $10,000,000 or less. It does not apply to timber or to property produced under a long-term contract. Special rules apply for farmers. The rules do not apply to property which is produced for use by the taxpayer if substantial construction has occurred before March 1, 1986.

In the case of inventory, some of the indirect costs which may not have been capitalized before the Tax Reform Act which must now be capitalized are administration expenses, taxes, depreciation, insurance costs, compensation paid to officers attributable to services, rework labor, and contributions to pension, stock bonus, and certain profit-sharing, annuity, or deferred compensation plans. Current deductions may be claimed for research and

experimental costs under section 174, intangible drilling costs for oil and gas and geothermal property, and mining exploration and development costs. Temporary Regulations section 1.263A-1T specifies other indirect costs that may be currently deducted and those that must be capitalized with respect to production or resale activities. For more information, see Temporary Regulations section 1.263A-1T.

Meals and entertainment.— The amount deductible for business meals and entertainment is generally limited to 80% of the amount otherwise allowable. In addition, meals may not be lavish or extravagant; a bona fide business discussion must occur during, immediately before, or immediately after the meal; and your employee must be present at the meal.

Special rules apply to deductions for tickets to entertainment activities. With the exception of certain charitable sporting events, the deduction for the cost of a ticket is limited to the face value of the ticket.

A limitation on the amount deductible for the rental of a luxury skybox is being phased in beginning in 1987 and will become fully effective in 1989. If the taxpayer rents a skybox in the same arena for more than one event, the deduction is limited to the sum of the face value on non-luxury box seats for the seats in the box covered by the lease. In the 1988 tax year, ⅔ is disallowed. Both the limitation on tickets to entertainment activities and the limitation on sky box rentals is calculated before the application of the 20% reduction required by section 274. See **Pub. 463,** Travel, Entertainment, and Gift Expenses, for details.

Transactions between related taxpayers.—
Generally, an accrual basis taxpayer may only deduct business expenses and interest owed to a related party in the year the payment is included in the income of the related party. See section 267 for limitation on deductions for unpaid expenses and interest.

Section 291 limitations.—Corporations may be required to adjust deductions for depletion of iron ore and coal, intangible drilling and exploration and development costs, bad debt deductions for financial institutions, and the amortizable basis of pollution control facilities. See section 291 to determine the amount of the adjustment.

Golden parachute payments.—A portion of the payments made by a corporation to key personnel that exceeds their usual compensation may not be deductible. This occurs when the corporation has an agreement (golden parachute) with these key employees to pay them these excessive amounts if control of the corporation changes. See section 280G for additional information.

Nondeductible Items

Certain interest expenses.—No deduction is allowed under section 163 for interest on the items described in section 807(c).

Addition to reserves for bad debts.—No deduction is allowed for an addition to reserves for bad debts. However, a deduction for specific bad debts is allowable if the requirements of section 166 are met.

Business startup expenses.—Business startup expenses are required to be capitalized unless an election is made to amortize them over a period of 60 months. See section 195.

Amortizable bond premiums.—No deduction for an amortizable bond premium is allowed under section 171. However, see section 811(b) for the rules relating to the treatment of amortizable bond premiums by life insurance companies.

Net operating loss deduction.—No net operating loss under section 172 is allowable for life insurance companies; instead, the provisions of section 810 relating to the operations loss deductions of life insurance companies apply. For more information, see the instructions for line 16, Schedule A.

Trademark and trade name expenses.—The deduction for amortization of trademark and trade name expenses has been repealed for expenses paid or incurred after 1986.

Foreign intangible drilling costs and mining and development costs.—Foreign intangible drilling costs and mining and development costs must either be added to the corporation's basis for cost depletion or be deducted ratably over a 10 year period. For more information, see sections 263(i), 616, and 617.

Certain travel and entertainment expenses.—Generally, a corporation cannot deduct an expense paid or incurred for a facility (such as a yacht or hunting lodge) that is used for an activity that is usually considered entertainment, amusement, or recreation. However, the corporation may be able to deduct such an expense if the amount is treated as compensation and reported on Form W-2 for an employee or on Form 1099-MISC for an independent contractor.

Line 16. Operations loss deduction.—Enter the amount of any operations loss deduction allowable under section 810. To determine the loss from operations for any taxable year, subtract line 7, Schedule A, from the total allowable deductions modified as follows: (1) No operations loss deduction is allowed; (2) You must figure the dividends-received deductions allowed by sections 243, 244, and 245 without regard to section 246(b), (as modified by section 805(a)(4)). This loss from operations then becomes an operations loss deduction to be carried back or over to another taxable year.

The operations loss deduction for a given taxable year is the total of the operations loss carryovers and carrybacks to that taxable year. Generally, you may carry a loss from operations back to each of the 3 years preceding the year of the loss and over to each of the 15 years following the year of the loss. Alternatively, you may make an irrevocable election to forego the carryback period and carry the loss over to each of the 15 years following the year of the loss. If the company is a new company for the loss year, the loss may be carried over to each of the 18 years following the year of the loss.

The amount of the loss that may be carried to each succeeding year in the carryback or carryover period is the amount by which the loss exceeds the sum of the offsets for each of the earlier tax years to which the loss may be carried. The term "offset" means, with respect to any taxable year, the increase in the operations loss deduction for the taxable year which reduces the life insurance company taxable income (computed without regard to the small life insurance company deduction) for the year to zero.

See section 844 for special loss carryover rules for an insurance company that has changed its form of organization or has had a change in the nature of its insurance business.

Note: *Section 810 is treated as a continuation of section 812 (as in effect before the enactment of the Tax Reform Act of 1984).*

Schedule B — Increase or (Decrease) in Reserves (Section 807)

Section 807 requires life insurance companies to determine whether certain reserves decreased or increased for the taxable year. A net decrease will be treated as includible in gross income, while a net increase will be treated as a deduction allowable in computing life insurance company taxable income.

The net increase or net decrease in reserves is figured by comparing the opening balance for reserves to the closing balance for reserves reduced by: (1) the policyholders' share of tax-exempt interest, and (2) for mutual life companies, the excess, if any, (shown on line 8, Schedule E) of the differential earnings amount over deductible policyholder dividends determined without regard to section 809. For rules dealing with the method of computing reserves on contracts where interest is guaranteed beyond the end of the tax year, see section 811(d).

Reserve adjustments are not treated as interest expenses for allocation purposes under section 864(c). See section 818(f).

Line 1. Life insurance reserves.—For rules dealing with the method of computing life insurance reserves, see sections 807(d) and (e). Section 807(d)(2)(B), as amended by the Act of 1987, provides that the interest rate used to compute life insurance reserves is the greater of the applicable Federal interest rate or the prevailing state assumed interest rate. See Revenue Ruling 88-16 I.R.B. 1988-10.

Line 2. Unearned premiums and unpaid losses.—For purposes of sections 807 and 805(a)(1) the amount of the unpaid losses (other than losses on life insurance contracts) shall be the amount of the discounted unpaid losses determined under section 846.

In general, section 846 provides that the amount of the discounted unpaid losses shall be computed separately by each line of business (except that the multiple peril lines shall be treated as a single line of business) and by each accident year and shall be equal to the present value of such losses determined by using: (1) the amount of the undiscounted unpaid losses; (2) the applicable interest rate; and (3) the applicable loss payment pattern. Special rules apply with respect to unpaid losses related to disability insurance (other than credit disability insurance), noncancelable accident and health insurance, cancelable accident and health insurance, and to the international and reinsurance lines of business. With regard to the special rules for discounting unpaid losses on accident

and health insurance (other than disability income insurance), unpaid losses are assumed to be paid in the middle of the year following the accident year.

As a rule, the amount of the undiscounted unpaid losses means the unpaid losses shown in the annual statement. However, unpaid losses must be adjusted to take into account estimated recoveries on account of salvage and reinsurance attributable to those losses. If the amounts shown in the annual statement were determined on a discounted basis and if the extent to which these losses were discounted can be determined on the basis of information disclosed on or with the annual statement, the amount of the undiscounted unpaid losses must be recomputed to eliminate any reduction attributable to such discounting. In no event can the amount of discounted unpaid losses determined under section 846 with respect to any line of business for an accident year exceed the aggregate amount of unpaid losses with respect to any line of business for an accident year as reported on the taxpayer's annual statement.

The applicable interest rate for each calendar year and the applicable loss payment pattern for each line of business are determined by the Secretary of the Treasury. The applicable interest rate for 1988, determined under section 846(c) for purposes of section 807, is 7.77%. (Rev. Rul. 88-16). The applicable interest rate for 1987 and earlier years is 7.20%. The applicable loss payment patterns have been published in Revenue Ruling 87-34, 1987-1 C.B. 168. The loss payment patterns and discount factors applicable for 1988 accident years are published in Revenue Ruling 88-63, 1988-31 I.R.B. 5. However, under the provisions of section 846(e), corporations having sufficient historical experience to determine a loss payment pattern may, under certain circumstances, elect to use their own. If such an election is made, the loss payment patterns will be based on the most recent calendar year for which an annual statement was filed before the beginning of the accident year. No election under section 846(e) shall apply to any international or reinsurance line of business. If the corporation elects to use its own loss payment pattern, be sure to check the "Yes" column for question Q in Schedule Q, Additional Information Required. For more information regarding this election, see section 846(e).

Section 807(d)(4)(A)(ii) permits an election to recompute Federal interest rate every 5 years. In general, a life insurance company would apply the greater of the applicable Federal interest rate (AFIR) or the prevailing state assumed interest rate for the calendar year in which the contract is issued and the following 4 calendar years. In the fifth calendar year after the calendar year in which the contract was issued, they would begin using the AFIR in effect for that fifth calendar year or the prevailing state assumed interest rate for the calendar year in which the contract was issued, whichever is greater. This rate would then remain in effect for the 4 years after that. For each subsequent 5 year period a similar recomputation would be required. Once made, the election is effective for contracts issued during that calendar year and any subsequent years, and may only be revoked with the consent of the Secretary.

Note: *An insurance company's treatment of salvage in determining its paid and unpaid losses is a method of accounting for Federal income tax purposes. In general, companies that did not previously treat salvage in accordance with the provisions of section 1.832-4T must change their method of accounting for the first tax year beginning after December 31, 1987. The "Fresh Start" provision of section 1023(e) of the Tax Reform Act of 1986, is not applicable to the adjustments required as a result of such a change of method. See Temp. Reg. 1.832-4T(d)(1), and Announcement 88-99 1988-28 I.R.B. 38 .*

Note: *Any insurance company required to discount unpaid losses under section 846, is allowed an additional deduction. To claim an 847 deduction, include it on line 14, Schedule A and attach a schedule showing your computation. If this deduction is taken you* ***must*** *make a special estimated tax payment. See the instructions for line 14b for how to show this payment. See new section 847 for details.*

Line 3. Supplementary contracts.—Enter the amount (discounted at the appropriate rate of interest) necessary to satisfy the obligations under insurance and annuity contracts, but only if such obligations do not involve (at the time with respect to which the computation is made) life, accident, or health contingencies. For purposes of this item, the appropriate rate of interest is the higher of the prevailing State assumed interest rate as of the time such obligation first did not involve life, accident, or health contingencies or the rate of interest assumed by the company (as of such time) in determining the guaranteed benefit. In no case, however, shall the amount so determined for any contract be less than the net surrender value of such contract.

Line 4. Dividend accumulations and other amounts.—Enter the total dividend accumulations and other amounts held at interest in connection with insurance and annuity contracts.

Line 5. Advance premiums.—Enter the total premiums received in advance and liabilities for premium deposit funds.

Line 6. Special contingency reserves.—Enter the total reasonable special contingency reserves under contracts of group term life insurance or group accident and health insurance which are established and maintained for the provision of insurance on retired lives, for premium stabilization, or for a combination thereof.

Line 8. Increase (decrease) in reserves.—In figuring the amount shown on line 8, any decrease in reserves must be computed without any reduction of the closing balance of section 807 reserves by the policyholders' share of tax-exempt interest. See the instructions for line 2, Schedule A.

Note: *If the basis for determining the amount of any item referred to in section 807(c) (life insurance reserves, etc.) at the end of the tax year differs from the basis for the determination at the beginning of the tax year, see section 807(f).*

Schedule C—Gross Investment Income (Section 812(d))

Line 1. Interest.—Enter on line 1 the total taxable interest received or accrued during the tax year, less any amortization of premium, plus any accrual of discount required under section 811(b). The appropriate amortization of premium and accrual of discount attributable to the taxable year on bonds, notes, debentures, or other evidence of indebtedness held by a life insurance company should be determined: (a) in accordance with the method regularly employed by the company, if such method is reasonable, and (b) in all other cases, in accordance with regulations prescribed by the Secretary of the Treasury. Market discount is not required to be accrued under the provisions of section 811(b). Attach a statement showing the method and computation used.

Note: *The Technical Corrections and Miscellaneous Revenue Act of 1988 ("Act of 1988") amended section 1011(d) of the The Tax Reform Act of 1986 to increase the tax rate from 28% to 31.6% on any gain recognized by any insurance company from the redemption of any market discount bond issued before July 19, 1984 and acquired on or before September 25, 1985.*

Line 3. Gross rents.—Enter the gross rents received or accrued during the taxable year. Related expenses, such as repairs, taxes, and depreciation should be reported as "Other deductions" on line 14, Schedule A.

Line 4. Gross royalties.—Enter the gross royalties received or accrued during the taxable year. If you claim a deduction for depletion, report it on line 14, Schedule A.

Line 5. Leases, terminations, etc.—Enter the gross income received from entering into, altering, or terminating any lease, mortgage, or other instrument from which the company derives interest, rents, or royalties.

Line 7. Gross income from a trade or business other than insurance .—Enter the gross income from any business other than an insurance business carried on by the life insurance company, or by a partnership of which the life insurance company is a partner. Include on this line section 1245, section 1250, and other ordinary gains on assets used in a noninsurance business from Form 4797. See the instructions under "Sale of Assets used in a trade or business and involuntary conversions," above. If you claim expenses related to any business other than an insurance business, report them on line 14, Schedule A.

Line 9. Tax-exempt interest.—Enter the total amount of tax-exempt interest income received or accrued during the taxable year. Tax-exempt interest does not include interest received on securities acquisition loans as defined in section 133(b).

Line 11. 100% qualifying dividends.—Enter the total amount of dividends for which the percentage used to determine the deduction allowable under sections 243, 244, and 245(b) is 100%. Do not include dividends to the extent that they are funded with tax-exempt interest or dividends that would not qualify as 100% dividends in the hands of the taxpayer. See section 812(e).

Note: *Multi-tiered corporate arrangements cannot be used to change the character of the tax-exempt interest and dividends received in an attempt to avoid exclusion.*

Schedule E—Policyholder Dividends (Section 808)

The term "policyholder dividend" is defined as any dividend or similar distribution to policyholders in their capacity as such.

Policyholder dividends include all amounts paid or credited (including an increase in benefits) where the amount is not fixed in the contract but depends on the company's experience or the management's discretion, plus all excess interest, premium adjustments, and experience-rated refunds. Furthermore, under the provisions of section 808(e), any policyholder dividend which increases either the cash surrender value of the contract or other benefits payable under the contract, or which reduces the premium that otherwise has to be paid, is treated as having been paid to the policyholder and returned by the policyholder to the company as a premium. When this happens, such amounts must be reported as income on line 1, Schedule A.

Generally, a company's deduction for policyholder dividends is the amount actually paid or accrued during the taxable year. However, mutual life insurance companies must reduce this amount by the differential earnings amount as determined under section 809. If a mutual life insurance company's differential earnings amount exceeds total policyholder dividends for the taxable year, the company must reduce its ending reserves by the amount of the excess.

Schedule F — Differential Earnings Amount (Section 809)

Section 809 requires mutual life insurance companies to reduce (but not below zero) their deduction for policyholder dividends by the differential earnings amount (as defined in section 809(a)(3)). If a mutual life insurance company's differential earnings amount exceeds the total policyholder dividends for a taxable year, the excess is treated as a reduction to the closing reserves balance for purposes of subsections (a) and (b) of section 807.

The differential earnings rate and the recomputed differential earnings rate for each taxable year are determined by the Secretary of the Treasury on the basis of information submitted by the 50 largest stock life insurance companies and all mutual life insurance companies. Neither the differential earnings rate nor the recomputed differential earnings rate can be a negative rate. See Notice 88-106, 1988-40 I.R.B. 17. The Service publishes both tentative and final differential earnings rates as this information is developed. For 1986, the tentative differential earnings rate was 10.837% and the final differential rate was 10.539%. The tentative recomputed differential earnings for 1986 is zero and the tentative differential earnings rate for 1987 is 3.647%. The final differential earnings rate for 1987 is 3.676% (Rev. Rul. 88-80).

To compute the differential earnings amount for 1988, multiply the average equity base (line 14, Schedule F) by the differential earnings rate for 1988. Enter the result on line 15, Schedule F. When determining the equity base, no item should be taken into account more than once.

See section 809 for definitions, computational information, transitional rules, and special adjustments that may be required.

Schedule G — Dividend Income and Dividends-Received Deduction

Line 1, column (a).—Enter dividends (except those received on debt-financed stock acquired after July 18, 1984) received from less-than-20%-owned domestic corporations subject to income tax and that qualify for the deduction allowable under section 243(a)(1).

Include on line 1, column (a), taxable distributions from an IC-DISC or former DISC that are designated as being eligible for the section 243(a)(1) deduction and certain dividends of Federal Home Loan Banks (see section 246(a)(2)). For dividends received from a regulated investment company, see section 854 for the amount that qualifies for the deduction.

So-called dividends or earnings received from mutual savings banks, money market certificates, etc., are really interest and should not be treated as dividends.

Line 2, column (a).—Enter dividends (except those received on debt-financed stock acquired after July 18, 1984) received from 20%-or-more-owned domestic corporations subject to income tax and that qualify for the deduction allowable under section 243(c)(1).

Line 3, column (a).—Enter dividends on debt-financed stock (acquired after July 18, 1984) received from domestic and foreign corporations subject to income tax and that would otherwise be subject to the dividends-received deduction under section 243(a)(1) or 245(a). Generally, debt-financed stock is stock that the corporation acquired and in doing so, incurred a debt (for example, it borrowed money to buy the stock).

Line 4, column (a).—Enter dividends received on the preferred stock of a less-than-20%-owned public utility that is subject to income tax and is allowed the deduction provided in section 247 for dividends paid.

Line 5, column (a).—Enter dividends received on the preferred stock of a 20%-or-more-owned-public utility that is subject to income tax and is allowed the deduction provided in section 247.

Line 6, column (a).—Enter the U.S. source portion of dividends received from less-than-20%-owned foreign corporations and that qualify for the 70% deduction under section 245(a). To qualify for the 70% deduction, the corporation must own at least 10% of the foreign corporation's stock by vote and value. Also enter on line 6, column (a), dividends received from a foreign sales corporation (FSC) that are attributable to income treated as effectively connected with the conduct of a trade or business within the U.S. (excluding foreign trade income) and that qualify for the 70% deduction provided in section 245(c)(1)(B).

Line 7, column (a).—Enter the U.S. source portion of dividends received from 20%-or-more-owned foreign corporations and that qualify for the 80% deduction under section 245(a). Also enter on line 6, column (a), dividends received from a foreign sales corporation (FSC) that are attributable to income treated as effectively connected with the conduct of a trade or business within the U.S. (excluding foreign trade income) and that qualify for the 80% deduction provided in sections 245(c)(1)(B) and 243(c)(2).

Line 8, column (a).—Enter dividends received from wholly owned foreign subsidiaries that qualify for the 100% deduction under section 245(b), but only to the extent that such dividends are distributed out of tax-exempt interest or out of dividends which do not qualify as 100% dividends. In general, the deduction under section 245(b) applies to dividends paid out of the earnings and profits of a foreign corporation for a tax year during which: (1) all of its outstanding stock is owned (directly or indirectly) by the domestic corporation receiving the dividend, and (2) all of its gross income from all sources is effectively connected with the conduct of a trade or business within the U.S. Also include on line 8, column (a), all dividends received from a FSC that are attributable to export sales income and that qualify for the 100% deduction under section 245(c). Do not include dividends received from a life insurance company.

Line 9, column (a).—Enter dividends that qualify for the 100% dividends-received deduction under section 243(a)(3) and that are subject to the elective provisions of section 243(b), but only to the extent that such dividends are distributed out of tax-exempt interest or out of dividends that do not qualify as 100% dividends. Do not include dividends received from a life insurance company.

Line 3, columns (b) and (c).—Dividends received on debt-financed stock are not entitled to the full 70% or 80% dividends-received deduction. Instead, the 70% or 80% deduction is reduced under the provisions of section 246A by a percentage that is related to the amount of debt incurred to acquire the stock. Also see section 245(a) before making this computation for an additional limitation which applies to dividends received from foreign corporations. For more information, see section 246A. Attach a schedule showing how the dividends-received deduction on debt-financed stock was computed.

Line 4, columns (b) and (c).—For dividends received on certain preferred stock of less-than-20%-owned public utilities, the dividends-received deduction percentage is 41.176%.

Multiply the dividends received by the proper percentage and enter the total in line 4, column (c).

Line 5, columns (b) and (c).—For dividends received on certain preferred stock of 20%-or-more-owned public utilities, the dividends-received deduction percentage is 47.059%.

Line 6, columns (b) and (c).—The dividends-received deduction percentages for line 6 are: (1) 70% for dividends from foreign corporations allowed the deduction under section 245(a); and (2) 70% for dividends from certain FSCs for which the deduction is allowed under section 245(c)(1)(B).

Note: *To qualify for the section 245(a) deduction, the corporation must own at least 10% of the stock of the foreign corporation by vote and value. The deduction is computed on the U.S. source portion of the dividends.*

Line 7, columns (b) and (c).—The dividends-received deduction percentages for line 7 are 80% for: (1) dividends from

foreign corporations allowed the deduction under section 245(a); and (2) dividends from certain FSCs for which the deduction is allowed under section 245(c)(1)(B).

Line 10, column (c)

Limitation on Dividends-received deduction worksheet

Generally, line 10 of column (c) may not exceed the amount from the worksheet below. However, in a year in which a loss from operations occurs, this limitation does not apply even if the loss is created by the dividends-received deduction. (See sections 246(b) and 810).

1. Add line 2, page 1, and line 7, Schedule A, less the total of lines 8 through 14, Schedule A, and without regard to: the small life insurance company deduction, the operations loss deduction, the dividends-received deduction (243(a)(1), 244(a), and 245), and any capital loss carryback to the current taxable year (1212(a)(1)) . . . _____
2. Enter the sum of lines 9 and 13, column (c) . . _____
3. Subtract line 2 from line 1 _____
4. Multiply the amount on line 3 by 80% . . . . _____
5. Enter the sum of the amounts on lines 2, 5, 7, and 8 of column (c) and the portion of the deduction on line 3 of column (c) that is attributable to dividends received from 20%-or-more-owned corporations . . . . _____
6. Enter the lesser of line 4 or line 5. (Do not complete the rest of this worksheet if line 5 is greater than line 4. Instead, enter the amount from line 6 on line 10 of column (c).) _____
7. Enter the total amount of dividends received from 20%-or-more-owned corporations . . . . _____
8. Subtract line 7 from line 3 _____
9. Multiply the amount on line 8 by 70% . . . _____
10. Subtract line 5 from line 10 of column (c) . . . _____
11. Enter the lesser of line 9 or line 10 . . . . _____
12. Dividends-received deduction after limitation (section 246(b)). Add the amounts on lines 6 and 11 and enter on line 10 of column (c) . . . . _____

Line 13, column (a).—Enter dividends that qualify for the 100% dividends-received deduction and that are not reported on line 8 or 9 because they were not distributed out of tax-exempt interest or out of dividends that do not qualify as 100% dividends, or because they were paid by a life insurance company.

Note: *Certain dividends received by a foreign corporation are not subject to proration. Attach a schedule showing your computation.*

Line 14, column (a).—Enter the total of other dividends received. Attach a schedule showing separately:

- Foreign dividends not reportable on lines 6, 7, 8, or 13. Exclude distributions of amounts constructively taxed under Subpart F (sections 951 through 964) in the current year or in earlier years.
- Income constructively received from controlled foreign corporations under Subpart F. This should equal the total amount reported in Schedule J of Form(s) 5471.
- Gross-up of dividends for taxes considered paid under sections 902 and 960.
- Dividends (other than capital gain and exempt-interest dividends) received from regulated investment companies that do not qualify for the dividends-received deduction.
- Dividends from tax-exempt organizations.
- Dividends (other than capital gain dividends) received from a real estate investment trust that, for the tax year of the trust in which the dividends are paid, qualify under sections 856 through 860.
- Dividends not eligible for the dividends-received deduction because of the stock's holding period or because of an obligation to make corresponding payments on similar stock.
- Any other taxable dividend income not properly reported above, including distributions under section 936(h)(4).

Note: *Two situations in which the dividends-received deduction will not be allowed on any share of stock are: (1) if the corporation held the stock with regard to which the dividends were issued for 45 days or less; or (2) to the extent that the corporation is under an obligation to make related payments for substantially similar or related property.*

Schedule H — Small Life Insurance Company Deduction (Section 806(a))

Schedule H is used to compute the small life insurance company deduction under section 806(a). To qualify for this deduction, a life insurance company must have both less than $15,000,000 of tentative life insurance company taxable income (tentative LICTI), and less than $500,000,000 in assets.

In computing the deduction, the tentative LICTI for any year must be determined without regard to all items attributable to noninsurance businesses. In general, the term "noninsurance business" means any activity which is not an insurance business. However, under the provisions of section 806(b)(3)(B), any activity which is not an insurance business shall be treated as an insurance business if: (1) it is of a type traditionally carried on by life insurance companies for investment purposes, but only if the carrying on of such activity (other than in the case of real estate) does not constitute the active conduct of a trade or business, or (2) it involves the performance of administrative services in connection with plans providing life insurance, pension, or accident and health benefits.

For purposes of the assets test, the assets of all members of a controlled group, as defined in section 806(c)(3), must be included, regardless of whether or not they are life insurance companies. For information regarding the valuation of assets, see the instructions for Schedule O, Part I.

The deduction for qualifying small life insurance companies is 60% of so much of the tentative LICTI for the taxable year as does not exceed $3,000,000. To the extent that tentative LICTI exceeds $3,000,000, the deduction is phased out. The reduction in the deduction is equal to 15% of so much of the tentative LICTI for the taxable year as exceeds $3,000,000.

Note: *In determining the amount of the small life insurance company deduction of a controlled group including an electing mutual company, for taxable years beginning after 1986 and before 1992, the taxable income of an electing mutual company must be taken into account in applying the phaseout of the small life insurance company deduction.*

Schedule I — Controlled Group Information (Section 806(c))

In computing the small life insurance company deduction, all life insurance company members of the same controlled group are treated as one life insurance company. Any small life insurance company deduction determined with respect to the group must be allocated among the life insurance companies in the group in proportion to their respective tentative LICTIs.

Schedule K — Company/ Policyholder Share Percentage (Section 812)

Schedule K is used to compute: (1) the company's share percentage to be used in determining the company's share of the dividends-received deduction under section 805(a)(4); and (2) the policyholders' share percentage to be used in determining the policyholders' share of tax-exempt interest for purposes of determining the increase or decrease in reserves under section 807.

In figuring the policyholders' and company's share percentages, carry out the computations to enough decimal places to ensure substantial accuracy and to eliminate any significant error in the resulting tax.

Lines 1–9.—Lines 1 through 9 are used to compute the investment income ratio. The investment income ratio is the ratio that gross investment income less policy interest bears to life insurance company gross income (including tax-exempt interest) less the amount of any increase in reserves. To compute the investment income ratio, complete lines 1 through 8 and then divide the amount on line 3 by the amount on line 8. Enter the result on line 9.

Note: *In computing the amount entered on line 8, any decrease in reserves must be computed without any reduction of the closing balance of section 807 reserve items by the policyholders' share of tax-exempt interest.*

Lines 10–19.—Lines 10 through 19 are used to compute the policyholders' share amount. First, lines 10 through 17 are completed to compute gross investment income's proportionate share of policyholder dividends on line 16. Line 16 is then multiplied by the investment income ratio. The result is added to the policy interest to compute the policyholders' share amount, which is entered on line 19.

Lines 20–26.—Lines 20 through 26 are used to compute both the company's share percentage and the policyholders' share percentage. First, net investment income is computed by multiplying gross investment income (line 20) by 90% or, in the case of gross investment income attributable to assets held in segregated asset accounts under variable contracts, by 95%. The policyholder share amount is subtracted from net investment income to compute the company's share of net investment income on line 23. The company's share percentage is computed on line 25 by dividing the company's share of net investment income (line 23) by net investment income. The policyholders' share percentage is figured by subtracting the company's share of net investment income from 100%.

Schedule L — Policy Interest (Section 812(b)(2))

Schedule L is used to compute the policy interest (as defined in section 812(b)(2)) for the taxable year. The policy interest is needed to calculate the company and policyholder share percentages in Schedule K.

Schedule M — Shareholders' Surplus Account (Section 815(c))

Section 815(c)(1) provides that each stock life insurance company (whether domestic or foreign) that had a policyholders' surplus account on December 31, 1983, will continue to maintain a shareholders' surplus account. Schedule M is used to calculate both the addition made to the shareholders' surplus account and the account's year-end balance as defined in section 815(c). In determining the tax liability shown on line 4, proper adjustments are to be made for any year in which the alternative minimum tax is imposed or the minimum tax credit has been taken.

Enter on line 6 all amounts treated under section 815 as distributions to shareholders. Any distribution to shareholders is treated as having been made first out of the shareholders' surplus account, to the extent thereof.

Schedule N — Policyholders' Surplus Account (Section 815(d))

Section 815(d)(1) provides that every stock life insurance company (whether domestic or foreign) that had an existing policyholders' surplus account on December 31, 1983, will continue to maintain the account. For tax years beginning after December 31, 1983, no additions can be made to this account; however, the account must be decreased by the amounts specified in section 815(d)(3). Further, section 815(f) provides that, in general, the provisions of subsections (d), (e), (f), and (g) of section 815 as in effect before the enactment of the Tax Reform Act of 1984 continue to be applicable in respect of any policyholders' surplus account for which there was a balance as of December 31,1983.

Amounts that are subtracted from the policyholders' surplus account for a taxable year are added to a corporation's taxable income and are subject to the tax imposed by section 801. Schedule N is used to compute both the ending balance in the policyholders' surplus account and the amount of any increase to taxable income.

Line 1.—Enter the beginning balance in the policyholders' surplus account. If the balance at the end of the preceding taxable year is different from the balance at the beginning of the current taxable year (for example, due to the provisions of section 815(d)(5) as in effect prior to the enactment of the Tax Reform Act of 1984), attach a schedule showing the adjustments made. Prior to the enactment of the Tax Reform Act of 1984, section 815(d)(5) provided that if any addition to the policyholders' surplus account increases or creates a loss from operations and part or all of the loss cannot be used in any other year to reduce the company's taxable income, then the loss will reduce the policyholders' surplus account at the time that the addition was made. In such a case, you must adjust the beginning balance of the policyholders' surplus account before any subtractions for the current taxable year are made.

Line 2a.—If the total direct and indirect distributions to shareholders during the taxable year exceeds the amount on Schedule M, line 5, enter the excess on line 2a.

Line 2b.—To compute the tax increase due to the amount entered on line 2a, you must: (1) subtract the corporation's tax rate from 100%; (2) divide the distributions on line 2a by the result of step 1; (3) subtract the amount on line 2a from the result of step 2; and (4) enter the result of step 3 on line 2b.

Line 2c.—To compute the amount to be entered on line 2c, you must: (1) determine the total amount to be subtracted from the policyholders' surplus account under sections 815(d)(1) and 815(d)(4) as they were in effect prior to the enactment of the Tax Reform Act of 1984 (do this only after you have subtracted the amounts on lines 2a and 2b from the beginning balance in the policyholders' surplus account); (2) add 100% to the corporation's tax rate; (3) divide the result of step 1 by the result of step 2; and (4) enter the result of step 3 on line 2c. You must also add the amount entered on line 2c to the shareholders' surplus account at the beginning of the next tax year.

Line 2d.—Subtract the result of step 3, line 2c, from the result of step 1, line 2c. Enter the result on line 2d.

Line 2e.—Enter the total amount to be subtracted from the policyholders' surplus account under the provisions of section 815(d)(2) as it was in effect prior to the enactment of the Tax Reform Act of 1984. At that time, section 815(d)(2) provided that if, for any taxable year, a taxpayer is not an insurance company, or if for any two successive taxable years a taxpayer is not a life insurance company, then any balance remaining in the policyholders' surplus account as of the end of the last taxable year that the taxpayer was a life insurance company shall be included in taxable income for such taxable year.

Line 3.—Enter the total of lines 2a through 2e on line 3; however, this total must be limited to the amount shown on line 1, Schedule N. Also enter this total on page 1, line 3.

Schedule O — Total Assets (Section 806(a)(3)(C)) and Total Insurance Liabilities (Section 842(b)(2)(B)(i))

All insurance companies required to file Form 1120L must complete Parts I and II of Schedule O.

Note: *Foreign insurance companies should report assets and insurance liabilities for their U.S. business only.*

Part I — Total Assets

For purposes of Schedule O, the term "assets" means all assets of the company. In valuing these assets, use fair market value for real property and stocks; for other assets, use the adjusted basis as determined under section 1011, and related sections, without regard to section 818(c). An interest in a partnership or trust is not itself treated as an asset of the company. Instead, the company is treated as actually owning its proportionate share of the assets held by the partnership or trust; the value of the company's share of these assets should be listed on line 3 of Schedule O.

Part II — Total Insurance Liabilities

Foreign insurance companies must maintain a certain surplus of U.S. assets over their U.S. insurance liabilities. The minimum required surplus is determined by multiplying their U.S. insurance liabilities by a percentage determined and proclaimed by the Secretary of the Treasury. The Secretary determines the percentage from data supplied by domestic insurance companies in Schedule O, Part II. For more information, see section 842.

For purposes of Schedule O, the term "total insurance liabilities" means the sum of the following amounts as of the end of the taxable year: (1) total reserves as defined in section 816(c); plus (2) the items referred to in paragraphs (3), (4), (5), and (6) of section 807(c), to the extent such amounts are not included in total reserves.

Enter each item on the appropriate line. Enter on line 9f any other amounts included in the definition of total insurance liabilities, but not described on this schedule.

Schedule P — Limitation on Noninsurance Losses (Section 806(b)(3)(C))

Section 806(b)(3)(C) provides that, in computing life insurance company taxable income, any loss from noninsurance business is limited to the lesser of 35% of the loss or 35% of life insurance company taxable income (computed by excluding any noninsurance loss included in Schedule A). Use Schedule P to compute any excess loss that must be added back to taxable income on page 1, line 2, Form 1120L. For more information on either the computation of the allowable loss deduction or on applicable carryback provisions, see section 1503(c).

Schedule Q — Additional Information Required

Be sure to answer questions G through S on page 7, Form 1120L. The instructions that follow are keyed to these questions.

1. Question J(2)(c). U.S. person.—The term "U.S. person" means: (1) A citizen or resident of the United States; (2) A domestic partnership; (3) A domestic corporation; or (4) Any estate or trust (other than a foreign estate or trust within the meaning of section 7701(a)(31)).

"Owner's country," for individuals, is the owner's country of residence. For all others, it is the country where incorporated, organized, created, or administered.

2. Question L. Foreign financial accounts.—Check the "Yes" box if either **a** or **b**, below, applies to the corporation; otherwise, check the "No" box:

(a) At any time during the year the corporation had an interest in or signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account); AND

- The combined value of the accounts was more than $10,000 at any time during the year; AND
- The account was NOT with a U.S. military banking facility operated by a U.S. financial institution.

(b) The corporation owns more than 50% of the stock in any corporation that would answer "Yes" to item a, above.

Get form **TD F 90-22.1,** Report of Foreign Bank and Financial Accounts, to see if the corporation is considered to have an interest in or signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account).

If "Yes" is checked for this question, file form TD F 90-22.1 by June 30, 1989, with the Department of the Treasury at the address shown on the form. Form TD F 90-22.1 is not a tax return, so do not file it with Form 1120L.

Form TD F 90-22.1 may be obtained from IRS Forms Distribution Centers.

Also, if "Yes" is checked for this question, write the name of the foreign country or countries. Attach a separate sheet if more space is needed.

3. Question P. —Report any tax-exempt interest received or accrued in the space provided. Include any exempt-interest dividends received as a shareholder in a mutual fund or other regulated investment company.

Schedule R — Reconciliation

All filers of Form 1120L must attach a schedule which reconciles their NAIC Annual Statement to their Form 1120L.

Schedule S — Compensation of Officers

Attach a schedule for all officers using the following columns:

1. Name of officer.
2. Social security number.
3. Percentage of time devoted to business.
4. Amount of compensation.

This information must be submitted by each member of an affiliated group included in a consolidated return.

Tax Computation Instructions — Page 1, lines 5–19

Any corporation that files Form 1120L should compute its tax using the tax computation worksheet. Members of a controlled group should see the instructions below for lines 5a and 5b before computing their tax.

Additional Tax

The worksheet below includes the computation of an additional 5% tax on the excess of a corporation's taxable income over the specified amount, which is $100,000. The limitation on the additional tax is $11,750.

Line 4. Total taxable income.—Generally, this is the sum of lines 1, 2, and 3 of page 1. However, if there is an amount entered on line 3, then even if lines 1 and 2 total less than zero, the amount entered on line 4 may not be less than the amount on line 3.

Line 5a.—Members of a controlled group, as defined in section 1563, are entitled to one $50,000 amount and one $25,000 amount (in that order) in each taxable income bracket on line 5a.

When a controlled group adopts or later amends an apportionment plan, each member must attach to its tax return a copy of its consent to this plan. The copy (or an attached statement) must show the part of the amount in each taxable income bracket apportioned to that member. There are other requirements as well. See Regulations section 1.1561-3(b) for the requirements and for the time and manner of making the consent.

Equal Apportionment Plan.—If no apportionment plan is adopted, the members of the controlled group must divide the amount in each taxable income bracket equally among themselves. For example, controlled group AB consists of corporation A and corporation B. They do not elect an apportionment plan. Therefore, corporation A is entitled to $25,000 (one-half of $50,000) in the taxable income bracket on line 5a(i) and $12,500 (one-half of $25,000) in the taxable income bracket on line 5a(ii). Corporation B is also entitled to the same amounts in each taxable income bracket.

Unequal Apportionment Plan.—Members of a controlled group may elect an unequal apportionment plan and divide the taxable income brackets as they wish. There is no need for consistency between taxable income brackets. Any member of the controlled group may be entitled to all, some, or none of the taxable income bracket. (But the total amount for all members of the controlled group cannot be more than the total amount in each taxable income bracket.)

Line 5b.—Members of a controlled group of corporations are treated as one corporation for figuring the additional 5% tax. If the additional tax applies, each member of the group must attach a schedule that shows the taxable income of the entire group, as well as how its portion of the additional tax (entered on line 5b) was figured.

Tax Computation Worksheet

1. Enter the taxable income (line 4, page 1) . . . . . _____
2. Enter line 1 above or your share of the $50,000 taxable income bracket, whichever is less . . . . . _____
3. Subtract line 2 from line 1 . . . . . _____
4. Enter line 3 or your share of the $25,000 taxable income bracket, whichever is less . . . . _____
5. Subtract line 4 from line 3 . . . . . _____
6. 15% of line 2 . . . . . _____
7. 25% of line 4 . . . . . _____
8. 34% of line 5 . . . . . _____
9. If the taxable income of the controlled group exceeds $100,000 enter the portion of the **lesser** of 5% of the excess over $100,000 or $11,750 that this member must pay . . . . . _____
10. Add lines 6 through 9. Enter here and on line 6, page 1 . . . . . _____

Line 6. Income Tax

If the amount on line 4 is:		The tax is:	
Over—	But not over—		Of the amount over—
0	$50,000	15%	0
$50,000	75,000	$7,500 + 25%	$50,000
75,000	-------	$13,750 + 34%	75,000

Line 7a. Foreign tax credit.—See **Form 1118,** Computation of Foreign Tax Credit — Corporations, for an explanation of when a corporation can take this credit for payment of income tax to a foreign country.

Line 7b. Other credits.—Possessions tax credit.—See **Form 5712,** Election To be Treated as a Possessions Corporation Under Section 936, for rules on how to elect to claim the possessions tax credit, and **Form 5735,** Computation of Possessions Corporation Tax Credit Under Section 936, to compute the credit. Include the credit in the amount shown on line 7b. On the line to the left of the entry space, write the amount of the credit and identify it as a section 936 credit.

Credit for fuel produced from a nonconventional source.—A credit is allowed for the sale of qualified fuels

produced from a nonconventional source. Section 29 contains a definition of qualified fuels, provisions for figuring the credit, and other special rules. Attach a separate schedule to the return showing the computation of the credit.

Orphan drug credit.—See section 28 and **Form 6765,** Credit for Increasing Research Activities (or for claiming the orphan drug credit), for an explanation of when a corporation can take this credit as well as how it is figured.

Line 7c. General business credit.—This credit is made up of the sum of the following credits:

Investment credit.—The investment credit was generally repealed for property placed in service after 1985. See **Form 3468,** Computation of Investment Credit, for exceptions.

Jobs credit.—The jobs credit, if elected, is allowed for hiring members of targeted groups during the tax year. See **Form 5884,** Jobs Credit, for definitions, special rules, and limitations.

Do not take an expense deduction for the part of the wages or salaries paid or incurred which is equal to the amount of the jobs credit determined without regard to the limitation based on the tax (section 38(c)).

Attach a schedule to Form 1120L to show how and where you reduced the salary and wage deduction(s). Show in this schedule the otherwise allowable deduction(s) before the reduction and the net amount actually deducted. Identify the line number, schedule, and page number of Form 1120L on which you made a reduction. If the reduction of salaries and wages is less than the jobs credit on Form 5884, explain the difference.

Alcohol fuel credit.—A corporation may be able to take a credit for alcohol used as fuel. Use **Form 6478,** Credit for Alcohol Used As Fuel, to figure the credit.

Credit for increasing research activities.—The credit for increasing research activities is now part of the general business credit. See Form 6765.

Low-income housing credit.— See section 42 and **Form 8586,** Low-Income Housing Credit.

Form 3800, General business credit. Enter on line 7c, page 1, the amount of the credit from Form 3800, and check the boxes indicating which forms are attached to the return. If the corporation is claiming only one of the above credits, it does not have to complete Form 3800. Instead, check the appropriate box and attach the form for which the credit is being taken. However, if the corporation has a carryforward or carryback of any of these credits, it must use Form 3800.

Line 7d. Credit for prior minimum tax.—If the corporation had an alternative minimum tax liability in a prior tax year beginning after 1986 but has no current year alternative minimum tax, it may be able to take the credit for prior year minimum tax. See **Form 8801,** Credit for Prior Year Minimum Tax, and section 53.

Line 10. Foreign corporations.— A foreign corporation carrying on an insurance business within the U.S. is taxable in the same manner as a domestic insurance company on its income effectively connected with the conduct of a trade or business within the U.S. See sections 842 and 897. Income from sources outside the U.S. from U.S. business is treated as effectively connected with the conduct of a trade or business within the U.S. For a definition of effectively connected income, see sections 864(c) and 897.

Generally, any other U.S. source income received by a foreign corporation that is not effectively connected with the conduct of a business within the U.S. is taxed at 30% (or at a lower treaty rate). (**Note:** *Interest received from certain portfolio debt investments that were issued after July 18, 1984, is no longer subject to the tax.)* See section 881. If you have this income, attach a schedule showing the kind and amount of income, the tax rate (30% or a lower treaty rate), and the amount of tax.

Additional taxes resulting from the net investment income adjustment may offset a company's 30 percent tax on U.S. source income. The tax reduction is determined by multiplying the 30 percent tax by the ratio of the amount of income adjustment to income subject to the 30 percent tax, computed without the exclusion for interest on state and local bonds or income exempted from taxation by treaty. Section 842(c)(3).

Attach a statement showing how you figured the reduction of section 881 tax. Enter the net tax imposed by section 881 on line 10, page 1.

Note: *Section 842(c)(1) requires that foreign life insurance companies make the investment income adjustment before claiming a small life insurance company deduction.*

Mutual life insurance companies are required to determine the amount of their policyholder dividends deduction by increasing their year-end equity base (under section 809) by the excess of their required U.S. assets over their mean assets held in the U.S. during that year. Section 842(c)(3).

Note: *Section 953(d) allows a foreign insurance company to elect to be taxed as a domestic corporation. Attach a statement if the corporation wishes to make the election. Include the additional tax required to be paid, on line 13. See section 953(d) for more details.*

Line 11. Recapture Taxes.—*Recapture of investment credit.* If property *is disposed of* or ceases to be qualified property before the end of the life-years used in computing the regular or energy investment credit, there may be a recapture of the credit. See **Form 4255,** Recapture of Investment Credit.

Recapture of low-income housing credit. If you must recapture part of the low-income housing credit because there has been a decrease in the qualified basis of a building from the prior year or if you disposed of the building or an ownership interest in it, see **Form 8611,** Recapture of Low-Income Housing Credit, and section 42(j). If you attached **Form 8693,** Low-Income Housing Credit Disposition Bond, write on the dotted line to the left of line 8, Schedule J, "Form 8693 attached."

Line 12a. Alternative minimum tax.—Attach **Form 4626,** Alternative Minimum Tax — Corporations, if the taxable income plus adjustments and tax preference items of the corporation exceed $40,000. See Form 4626 for details.

In general, the alternative minimum taxable income of any corporation for any taxable year beginning in 1987, 1988, or 1989 shall be increased by 50% of the amount by which the adjusted net book income exceeds the alternative minimum taxable income for the taxable year (determined without regard to this adjustment or the alternative tax net operating loss deduction). Section 56(f)(1).

Corporate book income is the net income or loss reflected in the taxpayer's applicable financial statements. Life insurance companies will generally use their annual statement as their starting point for computing the net book income adjustment (see section 56(f)(3) for the order of priority of financial statements). Adjustments are made to net income to reflect consolidated tax returns, remove Federal and foreign income taxes, and other adjustments. See Temp. Reg. 1.56-1T for more information.

Note: *Section 56(f)(2)(H) provides special rules for life insurance companies for the computation of the book income preference item. (1) In respect to mutual life insurance companies, only reduce adjusted net book income for policyholders' dividends to the extent that those dividends exceed the year's differential earnings amount under section 809. (2) Make additional adjustments as determined by the Secretary, to make the calculation of adjusted net book income consistent among insurance companies.*

Line 12b. Environmental tax.—The corporation may be liable for the environmental tax if the modified alternative minimum taxable income of the corporation exceeds $2,000,000. See Form 4626 for details.

Line 14b. 1988 estimated tax payments.—Include on this line all estimated tax payments for 1988. If a special estimated tax payment is required, enter on line 14b the net of your total estimated tax payments (total estimated tax payments made less the special estimated tax payment), and write on the dotted line to the left of the entry space "Net of SETP", and attach a schedule showing your computation. See section 847(2) for more information.

Line 14h. Other payments.—Credit for overpaid crude oil windfall profit tax.—A corporation that has overpaid its windfall profit tax may claim a credit on its income tax return. Use **Form 6249,** Computation of Overpaid Windfall Profit Tax, to figure the credit. Include the amount of the credit in the total for this line. Write in the margin, next to the entry on this line, the amount of the credit and identify it as "Overpaid Windfall Profit Tax." **Note:** *The Windfall profit tax does not apply to crude oil removed after August 22, 1988.*

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